Remarks by
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Farm Credit Administration
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Good Morning! Before I start, I just want to say thank you for asking me to join you this morning. When Andy asked me to come down, I thought that it was for beignets and coffee at Café DuMonde. I didn't realize that he was going to put me to work.

All jokes aside, you have a great leader in Andy Lowry. He has provided me personally and the Farm Credit Administration with unbiased and honest advice … and it has been appreciated … Andy, thank you.

Annual meetings are great, aren't they? You get to meet new people and renew old friendships. You get to catch up on what's happening back home with family and work. You get to share your successes and your challenges. And *you* even get to seek a little advice along the way. Since I have been coming to these meetings though, I have realized that above all there is one special topic farmers love to talk about at annual meetings, and that's the weather!

Well … since this is an annual meeting and since I'm here, I thought I'd do a little of all the above today, including talk about the weather.

I can tell you … I've got plenty of work to keep me busy and my family is fine, as I trust yours is … so what about the weather? Well … the weather in Washington has proven to be a bit stormy recently … and I can assure you, not only from the thunderstorms!

I'm sure you may know, the Farm Credit Bank of Texas has filed a lawsuit against the agency following our adoption of the loan participation final rule. There also seems to be a general discomfort within parts of the System regarding our proposed stockholder vote rule, which as you may know, is a parallel effort to our National Charter initiative.

And … as if those two issues weren't enough to keep us busy, House Banking Chairman Jim Leach, among with many bankers — and a few Farm Credit System institutions I might add — have criticized the process and policy of our National Charter initiative.

What a weather report! Thank God I have a raincoat … I think … and you may agree … I'm gonna need it!

Seriously though, I'd like to take a little time to walk through the issues.

First, with regard to the Texas lawsuit, I believe the central issue before the court will be whether the Farm Credit Act's exclusivity provisions not only extend to loan making … but, loan participations as well.

I think it is fair to say that the Texas Bank believes "yes," while the Farm Credit Administration's General Counsel advises the FCA Board, "no." Ultimately, the issue may turn on whether there is a legal distinction between loan making and loan participations. Only time and the court will tell. For the benefit of the System though, I hope the issue is decided quickly.

Secondly, with regard to FCA's proposed "stockholder vote" rule, the agency is currently evaluating the many comments we received. The comments ranged from questioning the agency's basic authority to require a vote, to concerns over the questions that would be posed to stockholders, the wording of the disclosures to stockholders, and the timeframes within which the votes must be held among other issues.

The feedback we have received will be very helpful as we fashion a final rule. I'd like to thank you for your comments.

While a final rule has not yet been adopted, I will share with you that the FCA Board believes that the stockholder-borrowers of Alabama, Louisiana, and Mississippi should have a vote in whether their territories should be opened up to allow other System institutions to compete for their business.

The statutory restrictions regarding these three states make a vote the most direct way of ensuring that stockholder-borrowers have a voice in their own future as a borrower and the future of their own association as an individual stockholder.

Finally, with regard to Chairman Leach's letter, some background may be helpful. The agency received the Chairman's letter about three weeks ago; and, in it, he raised concerns with both the process and policy surrounding our National Charter initiative.

With regard to process, the Chairman urged the agency to suspend our initiative until "proper processes involving formal rule making procedures are in place and until there is adequate opportunity for congressional scrutiny and oversight."

In our response to Chairman Leach, we noted that based upon his comments and those of others, the agency would publish the National Charter booklet in the *Federal Register* and invite interested parties to comment. Moreover, we promised to seriously consider and carefully weigh all substantive comments.

We also noted, however, that Farm Credit System institutions have always been able to request, and that the Farm Credit Administration has always been able to approve, charter changes. Our response went on to note that our General Counsel has advised us that the National Charter booklet is not subject to notice and comment rulemaking.

Indeed, the National Charter booklet that was issued is simply a vehicle by which FCA has communicated its willingness to accept applications for National Charters and the conditions under which we expect to grant them. The booklet does not set out any new rules or requirements for System institutions or other entities; nor does **it** require any System institution to apply for a National Charter.

With regard to the policy itself, the Chairman raised a number of issues. I'd like to respond to these, but before I do, it might be helpful to review how we got here first.

As many of you are aware, FCA has encouraged public discussion on ending the policy of exclusive charters in the System since 1994, when we asked for public comments on a proposed Board policy statement on non-exclusive charters. Moreover, the FCA Board consulted various experts throughout 1997 and into 1998 about how the System could respond to trends in agriculture and the financial markets. I'm sure you also recall that in July 1998, the FCA Board issued a philosophy statement announcing its support for removing regulatory geographic barriers for System institutions.

Why all the energy and effort by the FCA Board and so many others? What concerns have driven these studies, discussions, debates and policy statements in recent years? What is driving them today? Indeed, what will be driving them tomorrow?

Is the answer customer choice? Customer choice is certainly important, as is the seamless delivery of credit in the financial marketplace. Every hurdle in the financial marketplace that must be cleared by a customer or financial institution adds time and or costs. You know that in business, it's always important to make sure that the costs don't exceed the benefits. If they do, customers usually vote with their feet and go somewhere else.

From the agency's standpoint, a common thread in the studies, discussions, debates and ultimately even our philosophy statement, is that the System is a single sector lender with many FCS associations having high portfolio commodity concentrations because of the narrow geographic territories which they serve.

And, FCA is not the only one to recognize this risk. In fact, a 1990 report issued by the Secretary of the Treasury noted that the System is limited to a single business sector that is characterized by "high volatility." The report also highlighted that because FCS institutions provide credit in specific geographic regions, their "performance can rise and fall with the fortunes of a single crop or perhaps with those of a limited number of customers."

More recently, an October 1999 report issued by Moody's Investors Service noted that while the System has recovered from the severe financial stress in the 1980s, "the fundamental agricultural concentration remains [meaning within the FCS's asset portfolio], and this is a material and permanent credit risk."

I'm sure that as farmers, no one needs to convince you of the dangers of putting all, or even most of, your eggs in one basket … but the reality is the System, and even FCA, continue to wrestle with the risks that were reported more than a decade ago.

As for the FCA Board, we believe that rigid territorial constraints are unsafe and unsound for System institutions and hinder their capacity to serve agriculture and rural America now and in the coming decades.

It is upon this basis, that the FCA Board first pursued removing the "notice and consent" requirements in 4070 and now is willing, through our National Charter initiative, to consider granting expanded charters to System institutions.

With the preceding information in mind, I would like to address some of the policy concerns raised in Chairman Leach's recent letter.

The first concern the Chairman raised is that, "National Charters could translate into new safety and soundness risks as FCS institutions venture into geographical areas in which they may be inadequately prepared to assess and manage risk."

Our view, as stated previously, is that National Charters will enable System institutions to better manage the risks in their portfolios and thereby improve the safety and soundness of their operations. The added flexibility also will enable System institutions to meet the needs of agriculture and rural America now and in the future.

Since receiving authority to use formal enforcement powers in 1985, FCA has aggressively pushed institutions to build capital, strengthen loan underwriting standards, and institute effective management and internal controls.

I'm pleased to say that the System responded to our encouragement and, with the help of favorable economic conditions through most of the 1990s, the System today is safe and sound with a strong financial position. As the regulator, FCA must not only be concerned with the health of the System today, but tomorrow as well.

Another concern raised by Chairman Leach is that National Charters will lead to, "expansive activities outside of production agriculture."

It is important to note that National Charters will not provide any new lending authorities to System institutions. Whether or not FCS associations apply for a National Charter they will be bound by the same eligibility rules in their current lending operations.

We believe that the issuance of National Charters will result in a more competitive market for all eligible credit-worthy borrowers of the System. In fact, even borrowers who do not do business with the FCS will likely reap benefits from a more competitive marketplace.

Chairman Leach raises a concern that National Charters might dilute a System institution's commitment and capacity to serve local agricultural producers.

The FCA Board considers the System's responsibility toward their local customers so important that it has made development of a local service area plan an enforceable condition of implementing a National Charter. In fact, through our examination process we will review adherence to this condition and will take appropriate regulatory action if the conditions are not met.

Another concern raised by the Chairman is that large agricultural conglomerates will be advantaged at the expense of the family farmer.

The use of National charters does not change the System's statutory mandate to be a dependable source of credit for agriculture and rural America. Nor does it change the System's statutory mandate to place a special emphasis on assistance to young, beginning and small farmers. National Charters don't imply a change in the FCA Board's view of the System's basic responsibilities or statutory mandate.

Let there be no doubt that FCA will ensure through our examination process that the System meets its public policy mandate.

As each of you well know, FCS institutions must operate as borrower-owned financial cooperatives no matter how large a borrower's investment in the institution. Indeed, our regulations require that an association must operate under cooperative principles including, among other things, that shareholder votes be conducted on a one-member, one-vote basis.

Chairman Leach also raised concerns about "cherry picking" and predatory pricing.

We believe our regulatory and supervisory controls will constrain these practices in large part. Specifically, our regulatory capital requirement will automatically limit System institutions' ability to grow uncontrollably. Maybe even more importantly, boards of directors, who are elected by local borrower-shareholders, will be required to develop new business plans with a special focus on service to local areas and encouraged to report accomplishments annually to shareholders.

FCA intends to use its supervisory authority to monitor lending both inside and outside the local service area. This will be done by issuing new instructions for our quarterly call reports, which will include routine summary activity reports. We also expect existing local shareholders to watch closely the amount of business their boards of directors permit outside their local area.

It is true that in a competitive marketplace, however, we should expect to see some movement of customers from one institution to another as they seek the best alternative. At the same time though, we should expect to see institutions respond by providing better value through a combination of price and service — to attract and retain customers.

While FCA intends to be diligent in its regulatory and supervisory efforts, it is important to note that no amount of regulatory or supervisory involvement will change the fundamental truth that competition is a contact sport. Working within and respecting the dynamics of the marketplace, a regulator should not prevent or stifle competition, but rather focus on ensuring healthy and fair competition for the benefit of consumers. I can assure you … FCA will do this.

In summary, FCA believes that the removal of existing territorial constraints will enable System institutions to enhance the safety and soundness of their operations by diversifying the geographic and commodity mixes in their loan portfolios. Moreover, removing territorial constraints will improve the seamless delivery of credit to agricultural producers all across America.

Furthermore, we believe that the risks associated with increased competition arising from the changing financial markets of the new century, including the removal of territorial boundaries, are manageable. The Farm Credit System is financially strong and we have the necessary regulations, capital requirements, supervisory tools and oversight strategies to keep it safe with minimal risk to the public at no cost to the taxpayers.

Well, there you have it. That's the weather report from Washington.

I am confident that FCA's National Charter initiative is a rational, reasonable and responsible regulatory course of action in light of the geographic and commodity concentration risks highlighted in the reports by the Secretary of the Treasury, Moody's Investors Service and many others. These are the same risks that you and I know are all too real.

I appreciate the opportunity to speak with you this morning. If you have any questions, I'd be happy to try and answer them now.

Again, thank you and God bless.